

MULTIMEDIA



UNIVERSITY

STUDENT ID NO

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MULTIMEDIA UNIVERSITY

FINAL EXAMINATION

TRIMESTER 1833, 2018/2019

BFE8014 – GLOBAL FINANCIAL ECONOMICS (DBA)

27 MARCH 2019
10.00 a.m. to 1.00 p.m.
(3 Hours)

INSTRUCTIONS TO STUDENTS

1. This question paper consists of **FOUR (4)** printed pages, excluding cover page, of **TWO (2)** sections, **SECTION A** and **SECTION B**.
2. **Section A** consist of **TWO (2)** structure questions and **Section B** consist of **One (1)** case study.
3. Marks are shown for each question.
4. Write all your answers in the answer booklet provided.
5. Answer **ALL** questions.

Answer ALL questions.

SECTION A: STRUCTURED QUESTIONS (60 MARKS)

Question One (30 marks)

- (a) Provide three explanation on the application of the *Principles of Comparative Advantage* in international trade. (12 marks)
- (b) Explain the J-curve effect a country's balance of trade due to a depreciation of its currency. (8 marks)
- (c) We often read in the newspaper that the dollar is strong because U.S. interest rates are high. Explain this statement using the foreign exchange market analysis of asset demand approach. *Hint : you have to compare between two countries.* (10 marks)

Question Two (30 marks)

- (a) Evaluate sector rotation and identify preferred stocks or industry in each phase of the business cycle. Show them in a diagram by illustrate phases and industry. (14 marks)
- (a) The risk-free rate of return is 9 percent, and the expected return for the stock market is 16 percent. Essential Berhad has a beta of 1.2, and investors expect dividends and earnings to grow at an 8 percent rate per year. The current dividend is RM1.25, and the payout ratio is 50 percent. You are required to compute the followings:
 - (i) Calculate the price earnings (P/E) ratio for Essential Berhad. (3 marks)
 - (ii) Estimate the price of the stock for the next year using the multiplier model. (3 marks)
- (b) Assuming you are the vice president of Investment Division in one of renowned investment companies in Kuala Lumpur. You are required to formulate investment strategies and subsequently build a well-diversified portfolio for your investors in view of weak global economic outlook and challenging domestic economic environment in Malaysia after new Pakatan Harapan government. Provide justifications on how to form the well-diversified portfolio and investment strategies proposed. (10 marks)

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SECTION B: CASE STUDY (40 MARKS)

Read the extract of an article below and answer the following questions.

Forbes U.S.-China Trade War Boosts Fast-Growing Southeast Asia

By Vinnie Lauria
19 February 2019

Trade tensions between the U.S. and China are adding rocket fuel to the liftoff of Southeast Asia's economies. American tariffs on Chinese-made goods have sped the shift of contract manufacturing to ASEAN (Association of Southeast Asian Nations) countries, such as Vietnam and Thailand. The increase in foreign direct investment into the 10-nation regional trading bloc has been underway for a number of years, however, the trade war continues to drive even more capital into the region. Nikkei just published an article this month titled: "Southeast Asia bucks trend of sinking global foreign investment". A recent article in The Economist also highlights that "[U.S.-China] trade tensions are boosting activity in Southeast Asia."

"We are ready to grab the opportunity," Vietnam's Prime Minister Nguyen Xuan Phuc told Bloomberg in January. His country has a head start. Vietnam began making athletic shoes and sportswear for Adidas, Nike and other firms in the 1990s. Samsung now makes most of its mobile phones in Vietnam—amazingly, the nation has become the chief source for the world's largest phone producer, while the company is Vietnam's largest employer. And last fall the Chinese acoustics manufacturer Goertek announced that its production of Apple's AirPods wireless headphones will move to Vietnam, because of the trade war.

Thailand has growing clusters of vehicle assembly plants for Japanese, U.S., and Chinese auto companies, while also making components for tier 1 suppliers. Panasonic is joining the latter by shifting production of auto stereos from China. Meanwhile, the Thai electronics maker SVI has been sifting through requests from firms which, until now, had their work done in China. "The trade war is good for us," SVI's chief executive, Pongsak Lothongkam, said to *Business Insider*. "We have been approached by so many companies that we have to prioritize."

Not all of the movement from China to Southeast Asia is in high-tech or high-value goods. Cambodia snared bicycle production for U.S.-based Kent International.

But the shift is on. In 2012, Japanese firms had more direct investment and more personnel on the ground in China than in ASEAN, but the picture has flipped rapidly. Numbers from 2017 showed Japan investing \$22 billion in ASEAN versus just \$9.6 billion in China, while Japan's Foreign Ministry reported that roughly 83,000 expats are working in ASEAN, surpassing the 70,000 in China.

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As we witnessed in China, the growth in the manufacturing economy contributed to 87% of private sector R&D in the early years, not only promoting innovation and productivity in the country but subsequently creating a budding technology sector for future growth. This manufacturing shift towards the ASEAN region will mean more Southeast Asians working with and learning about advanced technology and more prosperous societies creating in-country consumer demand.

Which countries are poised for the greatest takeoff? Many observers favour Vietnam, which already exports vigorously (\$94 billion in electrical and electronics goods alone in 2017), offers a large workforce (population over 95 million, skewed young), and has worked to build good trade relations globally. But all ASEAN nations stand to gain from increased export manufacturing. Japan's Nomura Group sees significant upside for Malaysia, Thailand, The Philippines, Indonesia, Singapore, Cambodia and Vietnam.

Certainly, challenges still loom. Tech skills will need to improve in many ASEAN locales, including places like Vietnam and Thailand, where low unemployment means the most talented workers at present are already taken. Infrastructure build-out across the region will be needed, too. ASEAN countries are facing an increasing infrastructure deficit mainly due to rapid urbanization and population growth. The World Economic Forum, in a 2018 white paper co-authored with A.T. Kearney, urged the ASEAN nations to collaborate on issues like these to achieve full "readiness" for production growth.

As a whole, Southeast Asia is not entirely safe from the effects of the U.S.-China trade war. The benefits mentioned above might take a long time to fully come into effect and until then, the region may suffer in the short run from lower trade volumes and a lack of investor confidence. Given both the U.S. and China are major export markets for Southeast Asia, lower trade volumes from China could negatively affect countries that are more reliant on international trade, like Singapore, Malaysia, Thailand and Vietnam.

Tomorrow's ASEAN firms will have to compete on innovation, quality and ability to serve their home markets. Chinese firms have benefited from the immense size of their domestic market, and now rely on it increasingly. Keep in mind, though, that the ASEAN region combined population of 650 million is larger than either the EU or the U.S.-Mexico-Canada NAFTA trio. With the U.S.-China trade war now having its effects, Southeast Asia's economic potential is even more bullish than before.

Extracted from <https://www.forbes.com/sites/vinnielauria/2019/02/19/u-s-china-trade-war-boosts-fast-growing-southeast-asia-2/#315309ee6f5e>

Based on the extracted article above, answer the following questions.

- (a) Explain how ASEAN might benefit from US-China trade war. (16 marks)
- (b) Discuss the negative effect of US' trade protectionism on international trade. (16 marks)
- (c) Assume that China adopts a fixed exchange rate system. Explain the Bank of China's policy tools when Chinese Yuan is overvalued. (8 marks)

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SELECTED EQUATIONS

1) $R_i = \text{Risk Free Rate} + \beta_i (\text{Market Return} - \text{Risk Free Rate})$

2) $P/E = \frac{D/E}{k - g}$

3) $\text{Value} = P/E \times \text{Earnings per share (EPS)}$

4) $\text{Growth Rate} = \text{Retention Rate} \times \text{Return On Equity}$

5) $\text{Standard deviation} = \sqrt{\text{Variance}}$

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